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Posted on: Sunday, March 20, 2005

PUC vote puts sale of Verizon in limbo

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Verizon Hawaii probably would seek a new buyer should the proposed $1.65 billion sale of Hawai'is major phone company fall through, according to analysts who follow the company.

That would leave the company's future in limbo for another nine months or more — the time it would take for a potential new buyer to receive state regulatory approval.

The Hawai'i Public Utilities Commission Wednesday voted 2-1 to approve The Carlyle Group's acquisition of Verizon Hawaii, but with several new conditions to ensure consumers benefit despite the risks of creating a phone company loaded with debt.

These include: requiring the investment group to kick in more cash, restricting dividends to debt repayment and preventing the sale of the print directory business without PUC approval.

Carlyle, based in Washington, D.C., and Verizon Hawaii said they were reviewing the PUC's decision and could not comment on whether the deal will go through as planned.

Given the new conditions, it is not surprising Carlyle officials are still reviewing their options, said Joe Bonner, an analyst who follows Verizon Communications for Argus Research firm in New York.

"Sure, they sound fairly onerous," he said.

Should Carlyle back out, Verizon Hawaii would likely still be for sale, Bonner added.

"That's a logical conclusion," he said. "Verizon has been shedding some of their ancillary type businesses."

Drake Johnstone, an analyst with Richmond, Va.-based brokerage firm Davenport & Co., agreed that Hawai'i's phone company probably would remain on the auction block. However, it could be more difficult to sell the operation, given the PUC's position. That could hurt customers in the long run, Johnstone said.

"If the restrictions mean to the buyer that they don't get the desired return, it could mess up the deal," he said. "If the PUC makes it difficult for Verizon to sell it, they just might try to work that for cash flow and not invest (in the company)."

Carlyle had about 10 days from last Wednesday to appeal the PUC decision, though the company could seek an extension of that deadline. As of Friday, Carlyle had not asked the PUC to reconsider its opinion.

As defined under the PUC order, the sale of Verizon Hawaii — which would become Hawaiian Telcom — is expected to net Verizon Communications Inc. more than $850 million, while tripling the debt of the local phone company from $427 million to $1.39 billion.

Carlyle contends the sale will return management of the phone company to Hawai'i while boosting local employment and customer service. However, the state consumer advocate and others are concerned that the large debts of Hawaiian Telcom would increase the risk that the company could run into trouble if its financial targets aren't met. A foreclosure by lenders under such a scenario could affect customer service and rates along with employees' jobs.

It's unclear which PUC restrictions present the most concern for Carlyle, though analysts agreed that one condition prohibiting the sale of the print directory business would limit Hawaiian Telcom's flexibility and ability to generate a quick return from the acquisition.

Even though Carlyle has pledged not to raise rates, a sale of the print phone directory business would affect the phone company's overall earnings, which could result in higher phone rates in the future. In general, major telephone companies such as Verizon Communications have shed their print phone directories in selected markets.

"They generate revenues, (but) the problem is with wireless and voice over (Internet protocol calling), that revenue is declining," said Verizon analyst Bonner.

Other conditions placed on the sale include a requirement that Verizon give customers an estimated $20.70 credit on their bills and a rate-hike moratorium.

At the same time, the PUC order allows Verizon Communications to keep an estimated $280 million in excess money in a pension plan covering workers. The International Brotherhood of Electrical Workers Local 1357, which covers 1,300 Verizon Hawaii employees, said taking away the extra pension money could leave employees with less of a safety net and could result in higher rates for telephone customers if the pension becomes under-financed in the future.

For at least one Verizon Hawaii customer, the PUC's restrictions on the sale aren't enough to mitigate the risks.

"I guess I'm slightly negative on it," said Barry Graczyk, a customer in Makiki. "With the huge debt, I just don't see any advantage to consumers.

"It just seems the amount of the rebate is very small compared to the risk of reduced service and higher rates."

Meanwhile, the future of Hawai'i's major phone company remains unknown, which creates uncertainty for customers, employees and competitors.

"In any transaction, undecided is not a good end result for the community because if it's a 'yes,' we can prepare for that," said Yuka Nagashima, president for Internet and business services company LavaNet Inc. "If it's a 'no,' we can prepare for that, too."

Right now "We are sort of in a holding pattern," Nagashima said.

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